

Wednesday, 9 June 2021 | update

Kruk: accumulate (upgraded)

KRU.PW; KRU.WA | Financials, Poland

Borrowers show resilience amid pandemic

We upgrade Kruk to accumulate and we raise our target price to PLN 295.77 per share despite the recent rally. Kruk beat analysts' estimates with its quarterly results for the last two quarters thanks to the enduring capacity of borrowers to meet their payments, which has resulted in record-high recoveries and gains on fair value adjustments. Contrary to what we had predicted last September, the coronavirus crisis did not trigger a surge in bad debt; in fact, between March 2020 and March 2021, in Poland the non-performing loan portfolios of local banks shrunk by PLN 0.6 billion, thanks in no small part to government stimulus – as it turns out, Polish borrowers took the relief funds as an opportunity to pay down debt balances on an unexpected scale. On the one hand, the resulting decrease in delinquency rates indicates a contraction in the debt collection market, but on the other hand we currently expect a larger supply of bank NPLs than what we had predicted last September. Outside of Poland, Kruk has also registered improved collections on its portfolios in Italy and Spain, where we expect the Company to increase purchases moving forward. On the whole, we have raised our 2021 portfolio spend forecast for Kruk by a considerable 53%. With larger portfolios comes an increase in court fees for Kruk relative to voluntary settlements. All told, we have raised our FY2021-2023 earnings estimates for Kruk by 56%-33%, and after updating our valuation models we upgrade the stock to accumulate.

Discount valuation despite rally

Despite a 40% rally over the last three weeks, on FY2021 earnings forecasts Kruk stock is still trading at a discount of 16% at the current level relative to comparable debt collectors, many of whom have also registered strong performance over the last few months (Intrum +117%, B2H +123%, Arrow +281%, Hoist +54%). Relative to its book value, Kruk is trading at a premium of 57%-44%, but at the same time its net debt/equity ratio is two times lower on average than the ratios of competitors. Going forward, we believe Kruk will continue to catch up with sector peers given its above-average ROE (at approximately 20% today versus 12% average), combined with low leverage, positioning as the leader of a robust Polish debt collection market, and improved business in foreign markets, where local portfolios are starting to generate measurable returns.

Opportunities and risks

The rising returns on Italian and Spanish debt portfolios represent an opportunity for Kruk to grow its presence in these markets at a faster pace than we are currently assuming. On the risks side is intense competition, along with a potential rise in prices of debt portfolios that, historically, tends to occur after an economic rebound. Further, some analysts are anticipating a surge in insolvencies once pandemic relief measures expire. For Kruk, the short-term downside of this would be a decline in fair value valuation gains and collections, but as a long term benefit the supply of portfolios would increase. For the moment, given optimistic economic forecasts, in our view the opportunities ahead of Kruk outweigh the risks.

(PLN m)	2019	2020	2021E	2022E	2023E
revenue	1,251.1	1,138.0	1,471.1	1,574.4	1,674.5
gross profit	665.0	532.1	851.7	885.0	912.3
EBIT	440.3	332.3	595.5	612.2	624.1
net profit	277.1	81.0	449.2	466.7	456.7
ROE (%)	15.0	4.0	20.8	19.2	16.7
EPS (PLN)	14.6	4.3	23.6	24.5	24.0
BVPS (PLN)	103.2	107.5	119.4	136.2	152.0
P/E (x)	18.1	62.3	11.2	10.8	11.1
P/B (x)	2.6	2.5	2.2	2.0	1.7
Dividend yield	1.88%	0.01%	4.14%	2.95%	3.06%

current price	PLN 265.80
target price	PLN 295.77
mCap	PLN 5,053.1m
free float	PLN 5,053.1m
ADTV (3m)	PLN 9.6m

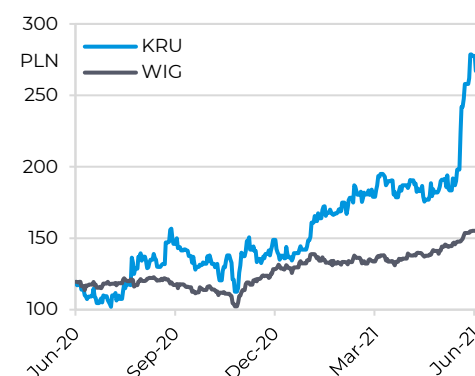
Shareholders

Piotr Krupa	9.61%
Other Management Board	0.70%
NN PTE	12.93%
PZU OFE	9.77%
Aviva OFE	9.41%
Allianz OFE	5.31%
Others	52.28%

About

Kruk is the leader of receivables management in Poland and Romania, focusing mainly on retail bank debt. Since 2015, the Company is also present in Germany and Italy. In the core markets of Poland, Italy, and Romania, Kruk's operations are organized into two complementary businesses: debt collection and debt purchases for own account.

KRU vs. WIG



company	target price		recommendation	
	new	old	new	old
Kruk	295.77	174.96	accumulate	hold
company	current price	target price	upside	
	Kruk	265.80	295.77	+11.3%
forecast update		2021E	2022E	2023E
EBITDA		+33.3%	+27.3%	+16.4%
EBIT		+36.6%	+29.6%	+17.4%
net profit		+56.1%	+47.6%	+32.7%

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List of abbreviations and ratios contained in the report:

EV (Enterprise Value) – Equity Value + Net Debt; **EBIT** – Earnings Before Interest and Taxes; **EBITDA** – EBIT + Depreciation & Amortisation; **Net Debt** – Borrowings + Debt Securities + Interest-Bearing Loans - Cash and Cash Equivalents; **P/E** (Price/Earnings) – Price Per Share Divided by Earnings Per Share; **P/CE** (Price to Cash Earnings) – Price Per Share Divided by Earnings + Depreciation & Amortisation; **P/B** (Price to Book Value) – Price Per Share Divided by Book Value Per Share; **P/CF** (Price to Cash Flow) – Price Divided by Cash Flow from Operations; **ROE** (Return on Equity) – Earnings Divided by Shareholders' Equity; **ROCE** (Return on Capital Employed) – EBIT x (Average Assets - Current Liabilities); **ROIC** (Return on Invested Capital) – EBIT x (1-Tax Rate) / (Average Equity + Minority Interest + Net Debt); **FCFF** (Free Cash Flow to Firm) – Cash Flow from Operations - CAPEX - Lease Payments; **FCFE** (Free Cash Flow to Equity) – Free Cash Flow to Firm - Net Interest Expense (incl. Debt + Leases) - Lease Payments

OVERWEIGHT (OW) – a rating which indicates that we expect a stock to outperform the broad market
NEUTRAL (N) – a rating which indicates that we expect the stock to perform in line with the broad market
UNDERWEIGHT (UW) – a rating which indicates that we expect the stock to underperform the broad market

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ACCUMULATE – we expect that the rate of return from an investment will range from 5% to 15%
HOLD – we expect that the rate of return from an investment will range from -5% to +5%
REDUCE – we expect that the rate of return from an investment will range from -5% to -15%
SELL – we expect that an investment will bear a loss greater than 15%

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NAV – valuation based on equity value, one of the most frequently used method in case of developing companies; the weak point of the method is that it does not factor in future changes in revenue/profits of a company.

mBank issued the following recommendations for Kruk in the 12 months prior to this publication:

Kruk

recommendation	hold	buy	buy
date issued	2021-02-02	2020-12-08	2020-09-03
target price (PLN)	174.96	174.96	183.17
price on rating day	168.30	142.30	156.70

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